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PUBLIC SCHOOL CAPITAL OUTLAY FUNDING EVENTS AND ACCOMPLISHMENTS

SUMMARY

In October 1999, the state's system of funding capital improvements for public schools was found unconstitutional. The court gave the state until mid-2000 "to establish and implement a uniform funding system for capital improvements" and "for correcting past inequities" in the funding program for New Mexico schools.

Through the collaborative efforts of many and the enactment of major legislation containing millions of dollars in appropriations, the district court in May 2002 found that the state had made significant progress in its response to the capital funding issues for public schools and that the proposed program based on adequacy standards presents the best method for funding projects and addressing the requirement for uniformity. This bulletin discusses the state's accomplishments and critical events leading up to the court decision.

ACCOMPLISHMENTS

Since 1999, the state has authorized substantial additional funding for **critical capital outlay projects** using supplemental severance tax bonds.

- In 2001, \$103 million was awarded to 51 school districts, \$41 million of which went to impact aid districts.
- In 2002, \$105 million was awarded to 49 school districts, \$48 million of which went to impact aid districts.

The legislature established the Deficiencies Corrections Unit, which has identified and validated over 8,000 **serious health and safety deficiencies** at all schools statewide, estimated to cost \$325 million to correct.

- \$150 million in senior and supplemental severance tax bonds and \$50 million from the state general fund were authorized in 2001 to address deficiencies.

As of September 12, 2002, \$42.7 million of the amount authorized has been awarded for 117 deficiency projects.

- There are plans to allocate the remaining \$157.3 million to address deficiencies by June 30, 2004.

The Public School Capital Outlay Council adopted statewide adequacy standards at its August 12, 2002 meeting. **Statewide adequacy standards** are those that "establish the minimum acceptable level for the physical condition and capacity of public school buildings, the educational suitability of educational facilities and the need for technological infrastructure" (Section 22-24-8 NMSA 1978).

The state has engaged a contractor to conduct a statewide needs assessment for all school facilities, and it is anticipated that the contractor's report will be submitted to the Public School Capital Outlay Council in December 2002.

The legislature has provided additional funding for school maintenance by increasing the state match or program guarantee amount under the Public School Capital Improvements Act.

- For FY 2002, \$11.2 million of state match or program guarantee was distributed to school districts.
- Supplemental severance tax bond proceeds have been made a permanent funding source for the match, thus freeing general fund dollars for other purposes.

The Public School Capital Outlay Task Force continues to meet and study the matter of funding public school capital outlay projects, and it will bring forth proposals to the legislature for consideration in 2003. (See 2001 Legislative Action below for current law.)

WHO'S WHO

Public School Capital Outlay Council (PSCOC): This is a statutory entity consisting of nine legislative, executive and public school representatives charged with identifying critical capital outlay needs for schools and investigating applications for and determining recipients of awards from the Public School Capital Outlay Fund (Sections 22-24-1 to 22-24-8 NMSA 1978).

State Department of Public Education (SDE), School Capital Outlay Unit: This is the entity that fulfills the support function of State Department of Public Education to the Public School Capital Outlay Council and facilitates the processing of school district requests for critical capital outlay funds, approval of disposition of school district property and approval of construction plans and specifications.

Deficiencies Corrections Unit (DCU): This is the staffing entity of the Public School Capital Outlay Council that validates outstanding serious health and safety deficiencies in public school buildings and grounds and oversees all aspects of project construction and management to correct the deficiencies (Section 22-24-4.2 NMSA 1978).

Public School Capital Outlay Task Force (PSCOTF): This is the short-term statutory entity, consisting of 21 university, legislative, executive, education and public representatives, that studies and evaluates progress mandated to address public school capital outlay funding and projects and that has monitored and assisted the Public School Capital Outlay Council in the development of statewide adequacy standards (Sections 22-24-1 to 22-24-8 NMSA 1978). It is scheduled to sunset on January 1, 2004.

BACKGROUND AND CRITICAL EVENTS

The Constitution

Article 12, Section 1 of the Constitution of New Mexico **guarantees a uniform system of free public schools to all children in the state.** Article 9, Section 11 provides that a school district may borrow money for the purchase or construction of school buildings or grounds but not in an amount greater than six percent of the assessed valuation of the school district. School districts have been unable, at certain times, to address critical school construction needs, leading to disparities among districts.

Public School Capital Outlay Funding Pre-2000

Laws 1971, Chapter 320 created the **Emergency Capital Outlay Fund** to provide state assistance to schools only if "**an emergency exists requiring immediate action**", and if the requesting district meets additional bonding and reappraisal requirements outlined in the laws.

Subsequently, the **Public School Capital Improvements Act**, Laws 1975 (S.S.), Chapter 5 (**commonly referred to as SB9**), provided funding for the **maintenance and repair** of schools by: (1) authorizing a local property tax levy of up to two dollars on each one thousand dollars of net taxable value of property allocated to the school district (Section 22-25-3 NMSA 1978); and (2) adding an additional **state match or program guarantee** of \$35.00 per program unit for each one dollar levy on each thousand dollars of net taxable value (Section 22-25-9 NMSA 1978). This minimal level of funding called the **state match or program guarantee** is calculated by multiplying a school district's 40th-day total program units by the matching dollar amount (\$35.00 per program unit) and the levy stated in the voter-approved resolution. When the local revenue generated by the levy is less than the program guarantee, a **state distribution** to the school district is awarded to achieve the guaranteed amount. In 2001, the program unit rate was increased to \$50.00 (Section 22-25-9 NMSA 1978).

Laws 1978, Chapter 152 enacted the **Public School Capital Outlay Act**, forming the basis of the **critical capital outlay program** operating today. It provided state assistance where a "**critical need exists requiring action**", and it limited eligibility to school districts bonded to at least 75 percent of capacity. The **Public School Capital Outlay Council** was created to approve awards to public schools from the Public School Capital Outlay Fund for critical capital outlay projects.

The State Department of Public Education created a task force in March 1998 that estimated there were \$1.5 billion in statewide public school capital outlay needs and recommended a new process for funding these needs (PSCOTF Report, 2000, 11). Since that time, estimates suggest the needs may reach \$2.5 billion, as reported to the Public School Capital Outlay Task Force in August 2002.

Shortly thereafter, in 1999, the legislature enacted several laws to address some of the identified capital outlay needs. Laws 1999 (1st S.S.), Chapter 6 created **new, supplemental severance tax bonds (STBs)** providing authorization for \$100 million for public school capital

outlay and \$25 million for higher education. These "second-lien STBs changed the 2-to-1 coverage for STBs to 1.6-to-1 coverage". Historically, the state had issued only senior STBs.

Enacted in 1961, the **Severance Tax Bonding Act** authorizes the issuance of severance tax bonds to finance public capital projects. Severance taxes are imposed on the severance of natural resources, such as oil, natural gas and coal, within this state, and the revenues are used to pay off the bonds issued. (An in-depth discussion of bonding is not provided in this bulletin.)

Laws 1999, Chapter 275 amended the **Public School Finance Act** to reduce the percentage of local revenue credit calculated in the **state equalization guarantee distribution for impact aid** and local property taxes from 95 percent to 75 percent. "The **state equalization guarantee distribution** is that amount of money distributed to each school district to ensure that the school district's **operating revenue**, including its local and federal revenues", as defined in Section 22-8-25 NMSA 1978, "is at least equal to the school district's program cost". Additional amendments mandated that 20 percent of the local revenue and impact aid receipts be expended for public school capital outlay. "**Impact aid**" refers to federal funds given by the federal government to the school districts whose tax bases are substantially impacted (reduced) by the presence of federal (non-taxable) lands, including Indian reservations (Section 22-8-25 NMSA 1978).

Court Challenge in 1998

The Zuni Public School District filed a lawsuit (referred to as the **Zuni** case) in January 1998 challenging the funding program for public schools. At issue was the provision for equalized funding for school district capital needs and the disparate abilities of districts to raise local revenues for schools (Zuni, 1998). The Gallup-McKinley County School District and the Grants-Cibola County School District were granted a motion to intervene in December 1998.

In October 1999, a state district court partial summary judgment in the **Zuni** case held that the system of funding capital improvements for New Mexico's schools was unconstitutional, and the court set a July 28, 2000 deadline for the state "to establish and implement a uniform funding system for capital improvements" and "for correcting existing past inequities" in the funding program for New Mexico schools. "The court also found that the disparity in bonding capacity, and differing taxable land

values among the school districts created a lack of uniformity for funding capital improvements" (Zuni, 1999).

2000 Legislative Session

During the regular session, amendments to the **Severance Tax Bonding Act** were enacted authorizing supplemental STBs for up to \$75 million for public schools (Laws 2000, Chapter 95). This provision was repealed in 2001 and replaced with a permanent funding stream.

2000 Second Special Session

Legislation amending the **Public School Capital Outlay Act** created a new framework for a statewide project-based capital funding program and a **state match distribution formula** for public school capital projects. Additionally, it required the Public School Capital Outlay Council to develop **statewide adequacy standards** (Laws 2000 (2nd S.S.), Chapter 19) to guide funding for public school capital projects.

Another \$400 million in supplemental STBs for public schools was authorized to be issued over 10 years (Laws 2000 (2nd S.S.), Chapter 11). The \$400 million and 10-year funding limitations were later repealed and replaced in 2001 when permanent funding was instituted with limitations based upon the state's severance tax bonding capacity. Furthermore, the amendments to the Public School Capital Outlay Act required that \$20 million of the bond revenue be **set aside for impact aid districts** annually in fiscal years 2001 through 2003.

In response to Senate Joint Memorial 21 of the same session, the Public School Capital Outlay Task Force was appointed to analyze funding options and make recommendations on a permanent revenue stream to address public school capital outlay needs and to study issues related to the impact aid credit and its relationship to the public school state equalization guarantee "formula" for funding public school operating costs. The Public School Capital Outlay Task Force findings and recommendations, released in December 2000, led to the enactment of ground-breaking legislation in 2001 (Highlights, 2001).

In April 2000, the district court found that the state had made some progress.

2001 Legislative Action

Laws 2001, Chapter 338 (referred to as **SB167**) embraced "the **legal concept of adequacy, rather than equity**, as the measure for interpreting the constitutional requirement of

a uniform system of free public schools" (Highlights, 2001). As recommended by the Public School Capital Outlay Task Force, SB167 included short- and long-term processes to remedy past inequities and to provide for an ongoing uniform public school capital projects funding program to replace and expand previous methods of funding. As mandated in the legislation, the Public School Capital Outlay Council developed adequacy standards by September 1, 2002 for use in making future allocations of funding.

During the **short-term** period covering fiscal years 2002-2004, serious health, safety and code deficiencies in the schools are to be addressed. SB167 created the **Deficiencies Corrections Unit** as part of the Public School Capital Outlay Council to administer the deficiencies program. The bill appropriated \$200 million to correct immediate **health and safety deficiencies** using 100 percent state dollars as follows: \$100 million in senior STBs, \$50 million in supplemental STBs and \$50 million from the general fund. It is anticipated that these funds will be fully allocated by 2004. Also, **the state match or program guarantee** for facilities maintenance under SB9 (the Public School Capital Improvements Act) was increased from \$35.00 to \$50.00 per program unit. For FY 2005 and after, an additional state match may be certified by the state superintendent of public instruction.

For the critical capital outlay program, SB167 reduced the requirement that school districts be indebted at not less than 75 percent of their capacity to **65 percent** of their capacity (Section 22-24-5 NMSA 1978); maintained the \$20 million set-aside of supplemental STB funds for allocation to impact aid districts for FY 2002 and FY 2003; explicitly recognized the need for space for full-day kindergarten and directed up to \$5 million per year be used for that purpose; appropriated \$2.3 million to complete a statewide needs assessment of public school facilities; and created the Public School Capital Outlay Task Force in statute to continue for three years.

SB167 replaced and expanded the supplemental STB funding established in 2000 with a **permanent** authorization to issue supplemental STBs for: (1) **SB9 state match or program guarantee** for public school maintenance and repair; and (2) standards-based capital outlay projects in an amount estimated at \$60 million to \$100 million per year (dependent upon oil and natural gas prices). The establishment of **permanent funding through STBs** is a very significant legislative commitment to funding public school capital outlay needs for the long term. Program funding for public school capital outlay

projects will be shared between the state and local districts on a formula basis and awarded based on the new **statewide adequacy standards**. All school districts will be eligible to apply for state funding in the 2003 cycle regardless of the level of bonded indebtedness; however, the amount of the state award will be based on the formula using relative tax base and local effort factors.

Special Master

In January 2002, a special master appointed by the district court in the **Zuni** case found that New Mexico's proposed program based on adequacy standards presents the best method for funding projects and addresses the requirement for uniformity; the state had made a substantial effort to rectify disparities and comply with the district court requirements for meeting adequacy standards; and direct legislative appropriations need to be taken into account in the funding formula. In a May 2002 district court ruling, the special master's report was adopted; however, the district judge reserved the right to hold status conferences to monitor and review progress in this area.

REFERENCE LIST

Articles 9 and 12 of the Constitution of New Mexico and the New Mexico Statutes.

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This document primarily contains information and excerpts from publications of the LCS and from reports and speeches by Paula Tackett and Janet Peacock that were prepared for the Public School Capital Outlay Task Force, the Legislative Finance Committee and the Legislative Education Study Committee. They are condensed here by Roxanna Knight. For more information, contact the Legislative Council Service at (505) 986-4600. This document does not represent a policy statement of the Legislative Council Service or its staff.

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